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GULF COAST REBUILDING

Observations on Federal Financial Implications

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Mr. Chairman and Members of the Committee:

I appreciate the opportunity to participate in today's hearing to discuss our preliminary observations on the federal financial implications of Gulf Coast rebuilding issues.¹ The Gulf Coast and the nation continue to face daunting rebuilding costs, uncertainty surrounding numerous decisions linked to the availability of federal funds, and the complexity of integrating multiple public and private decisions that will influence the future of the region. The size and scope of the devastation caused by the Gulf Coast hurricanes² presents the nation with unprecedented rebuilding challenges as well as opportunities to reexamine shared responsibility among all levels of government. Wide swaths of housing, infrastructure, and businesses were destroyed, leaving more than 1,500 people dead and hundreds of thousands of others displaced without shelter and employment. Our ongoing work in Mississippi, southern Louisiana, and New Orleans confirms that some communities still lack fulfillment of basic needs, such as schools, hospitals, and other infrastructure, while the doors of many businesses remain closed. Almost 2 years since the hurricanes made landfall, many Gulf Coast neighborhoods and communities still need to be rebuilt—some from the ground up.

Major decisions still need to be made regarding infrastructure, housing, levee protection, coastal restoration, and economic recovery, among other issues. All levels of government, together with the private and nonprofit sectors, will need to play a critical role in the process of choosing what, where, and how to rebuild. Agreeing on what the costs are, what rebuilding should be done and by whom, and who will bear the costs will be key to the overall rebuilding effort.

My testimony today will offer some preliminary observations on the federal financial implications of rebuilding efforts in the Gulf Coast. These observations may assist you in your oversight of these activities—now and over the longer term. I would like to: (1) place the federal assistance provided to date in the context of varied damage estimates for the Gulf Coast; and (2) discuss the key federal programs that provide rebuilding assistance, with an emphasis on Public Assistance (PA) and Community Development Block Grants (CDBG). In doing

¹This testimony updates and expands on GAO, *Gulf Coast Rebuilding: Preliminary Observations on Progress to Date and Challenges for the Future*, [GAO-07-574T](#) (Washington, D.C.: Apr. 12, 2007); and GAO, *Preliminary Information on Rebuilding Efforts in the Gulf Coast*, [GAO-07-809R](#) (Washington, D.C.: June 29, 2007).

²In this testimony, unless otherwise noted, we refer to Hurricanes Katrina, Rita, and Wilma collectively as the Gulf Coast hurricanes.

so, we will highlight aspects of Gulf Coast rebuilding likely to place continued demands on federal resources.

My statement is based largely on our completed and ongoing work in Washington, D.C., as well as Louisiana and Mississippi—the two states most directly affected by the Gulf Coast hurricanes. Specifically, we analyzed state and local documentation related to funding for rebuilding and interviewed state and local officials as well as representatives from nongovernmental organizations in these two states. We also interviewed various federal officials from the Federal Emergency Management Agency (FEMA), the Department of Housing and Urban Development (HUD), and the Coordinator of Federal Support for the Recovery and Rebuilding of the Gulf Coast Region³ within the Department of Homeland Security (DHS) and analyzed federal regulations and state policies regarding funding for the Gulf Coast. We performed our work in accordance with generally accepted government auditing standards.

Estimates Raise Questions Regarding Long-term Funding

The total long-term funding for helping the Gulf Coast recover from the 2005 hurricanes hinges on numerous factors including policy choices made at all levels of government, knowledge of spending across the federal government, and the multiple decisions required to transform the region. To understand the long-term federal financial implications of Gulf Coast rebuilding it is helpful to view potential federal assistance within the context of overall estimates of the damages incurred by the region. Although there are no definitive or authoritative estimates of the amount of federal funds that could be invested to rebuild the Gulf Coast, various estimates of aspects of rebuilding offer a sense of the long-term financial implications. For example, early damage estimates from the Congressional Budget Office (CBO) put capital losses from Hurricanes Katrina and Rita at a range of \$70 billion to \$130 billion⁴ while another estimate put losses solely from Hurricane Katrina—including capital losses—at more than \$150 billion.⁵ Further, the state of Louisiana has estimated that the economic effect on its state alone could reach \$200 billion. The exact costs of damages from the Gulf Coast

³Throughout this report and unless otherwise noted, we refer to this official as the Federal Coordinator for Gulf Coast Rebuilding.

⁴According to CBO, capital losses include housing, consumer durable goods, and energy, other private-sector, and government losses.

⁵This estimate includes damages only to commercial structures and equipment, residential structures and contents, electrical utilities, highways, sewer systems, and commercial revenue losses. For more information see, Mark L. Burton and Michael J. Hicks, Hurricane Katrina: *Preliminary Estimates of Commercial and Public Sector Damages* (Huntington, W.Va.: Marshall University, September 2005).

hurricanes may never be known, but will likely far surpass those from the three other costliest disasters in recent history—Hurricane Andrew in 1992, the 1994 Northridge earthquake, and the September 2001 terrorist attacks.⁶ These estimates raise important questions regarding how much additional assistance may be needed to continue to help the Gulf Coast rebuild, and who should be responsible for providing the related resources.

To respond to the Gulf Coast devastation, the federal government has already committed a historically high level of resources—more than \$116 billion—through an array of grants, loan subsidies, and tax relief and incentives. The bulk of this assistance was provided between September 2005 and May 2007 through five emergency supplemental appropriations.⁷ A substantial portion of this assistance was directed to emergency assistance and meeting short-term needs arising from the hurricanes, such as relocation assistance, emergency housing, immediate levee repair, and debris removal efforts. The Brookings Institution has estimated that approximately \$35 billion of the federal resources provided supports longer-term rebuilding efforts.⁸

The federal funding I have mentioned presents an informative, but likely incomplete picture of the federal government’s total financial investments to date. Tracking total funds provided for federal Gulf Coast rebuilding efforts requires knowledge of a host of programs administered by multiple federal agencies. We previously reported that the federal government does not have a governmentwide framework or mechanism in place to collect and consolidate

⁶According to CBO, losses from Hurricane Andrew—a Category 5 hurricane that struck the coast of Florida in 1992—totaled about \$38.5 billion in 2005 dollars. The earthquake that struck Northridge, California in 1994, which measured 6.7 on the Richter scale—resulted in \$48.7 billion in losses, as measured in 2005 dollars. Further, losses from the terrorist attacks on September 11, 2001, were estimated at \$87 billion in 2005 dollars, of which \$35.2 billion were privately insured losses.

⁷Pub. L. No. 109-61, 119 Stat. 1988 (Sept. 2, 2005); Pub. L. No. 109-62, 119 Stat. 1990 (Sept. 8, 2005); Pub. L. No. 109-148, 119 Stat. 2680 (Dec. 30, 2005); Pub. L. No. 109-234, 120 Stat. 418 (June 15, 2006); and Pub. L. No. 110-28, 121 Stat. 169 (May 25, 2007). In addition to these five supplemental appropriations acts, a number of authorizations and programs in multiple federal agencies provided assistance. Congress also increased the borrowing authority of the National Flood Insurance Program to cover the large number of hurricane-related claims. Pub. L. No. 109-65, 119 Stat. 1998 (Sept. 20, 2005); Pub. L. No. 109-106, 119 Stat. 2288 (Nov. 21, 2005); and Pub. L. No. 109-208, 120 Stat. 317 (Mar. 23, 2006). In addition, Congress passed the Gulf Opportunity Zone Act to provide tax relief benefits and incentives to affected individuals and businesses. Pub. L. No. 109-135, 119 Stat. 2577 (Dec. 21, 2005).

⁸Amy Liu, “Building a Better New Orleans: A Review of and Plan for Progress One Year after Hurricane Katrina.” Special Analysis in Metropolitan Policy (Washington, D.C.: The Brookings Institution, August 2006).

information from the individual federal agencies that received appropriations in emergency supplementals for hurricane relief and recovery efforts or to report on this information.⁹ It is important to provide transparency by collecting and publishing this information so that hurricane victims, affected states, and American taxpayers know how these funds are being spent. Until such a system is in place across the federal government, a complete picture of federal funding streams and their integration across agencies will remain lacking.

Demand for Federal Rebuilding Resources Likely to Continue

Demands for additional federal resources to rebuild the Gulf Coast are likely to continue, despite the substantial federal funding provided to date. The bulk of federal rebuilding assistance provided to the Gulf Coast states funds two key programs—FEMA’s Public Assistance (PA) program and HUD’s Community Development Block Grant (CDBG) program. These two programs follow different funding models. PA provides funding for restoration of the region’s infrastructure on a project-by-project basis involving an assessment of specific proposals to determine eligibility. In contrast, CDBG affords broad discretion and flexibility to states and localities for restoration of the region’s livable housing. In addition to funding PA and CDBG, the federal government’s recovery and rebuilding assistance also includes payouts from the National Flood Insurance Program (NFIP) as well as funds for levee restoration and repair, coastal wetlands and barrier islands restoration, and benefits provided through Gulf Opportunity Zone (GO Zone) tax expenditures.

Public Assistance Program Faces Increased Costs

The PA Grant program provides assistance to state and local governments and eligible nonprofit organizations on a project-by-project basis for emergency work (e.g., removal of debris and emergency protective measures) and permanent work (e.g., repairing roads, reconstructing buildings, and reestablishing utilities).¹⁰ After the President declares a disaster, a state becomes eligible for federal PA funds through FEMA’s Disaster Relief Fund. Officials at the local, state, and federal level are involved in the PA process in a variety of ways. The grant

⁹GAO, *Disaster Relief: Governmentwide Framework Needed to Collect and Consolidate Information to Report on Billions in Federal Funding for the 2005 Gulf Coast Hurricanes*, [GAO-06-834](#) (Washington, D.C.: Sept. 6, 2006).

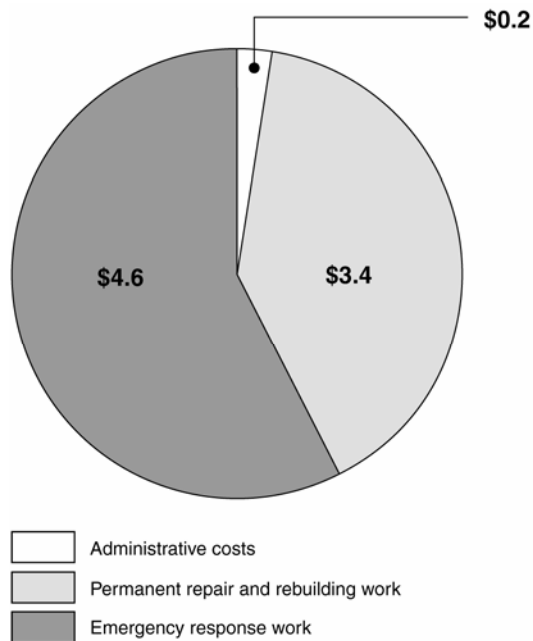
¹⁰PA is typically a cost-share program between the federal and state and local governments. However, for Hurricanes Katrina and Rita, the state and local match requirements were waived for eligible emergency work in the immediate aftermath of the storms and the federal government provided 100 percent funding. In addition, Congress recently passed, and the President signed into law, legislation to adjust the federal cost-share of certain eligible rebuilding projects to 100 percent. U.S. Troop Readiness, Veterans’ Care, Katrina Recovery, and Iraq Accountability Appropriations Act, 2007, Pub. L. No. 110-28 § 4501, 121 Stat. 112, 156 (May 25, 2007).

applicant, such as a local government or nonprofit organization, works with state and FEMA officials to develop a scope of work and cost estimate for each project that is documented in individual project worksheets. In addition to documenting scope of work and cost considerations, each project worksheet is reviewed by FEMA and the state to determine whether the applicant and type of facility are eligible for funding. Once approved, funds are obligated, that is, made available, to the state. PA generally operates on a reimbursement basis. Reimbursement for small projects (less than \$59,700) are made based on the project's estimated costs, while large projects (more than \$59,700) are reimbursed based upon actual eligible costs when they are incurred.¹¹

As of the middle of July 2007, FEMA had approved a total of 67,253 project worksheets for emergency and permanent work, making available about \$8.2 billion in PA grants to the states of Louisiana, Mississippi, Texas, and Alabama. A smaller portion of PA program funds are going toward longer-term rebuilding activities than emergency work. Of the approximately \$8.2 billion made available to the Gulf Coast states overall, about \$3.4 billion (41 percent) is for permanent work such as repairing and rebuilding schools and hospitals and reestablishing sewer and water systems, while about \$4.6 billion (56 percent) is for emergency response work such as clearing roads for access and sandbagging low-lying areas. The remaining amount of PA funds, about \$0.2 billion (3 percent) is for administrative costs. (See fig. 1.) Of the funds made available by FEMA to the states for permanent rebuilding, localities have only received a portion of these funds since many projects have not yet been completed. Specifically, in Louisiana and Mississippi, 26 and 22 percent of obligated funds, respectively, have been paid by the state to applicants for these projects.

¹¹Under the Robert T. Stafford Disaster Relief and Emergency Assistance Act (Stafford Act), project funds cover the restoration or rebuilding of damaged facilities to their predisaster design and capacity. 42 U.S.C. § 5172(e)(1)(A)(i).

Figure 1: Breakdown of Public Assistance Grants Made Available to the Gulf Coast States as of the middle of July 2007 (billions of dollars)



Source: GAO analysis of FEMA data.

Note: Dates vary for the most recent data available from the states. Data included are as of the following dates: Alabama, July 19, 2007; Louisiana, July 19, 2007; Mississippi, July 19, 2007; and Texas, July 19, 2007.

The total cost of PA funding for the Gulf Coast hurricanes will likely exceed the approximately \$8.2 billion already made available to the states for two reasons: (1) the funds do not reflect all current and future projects, and (2) the cost of some of these projects will likely be higher than FEMA's original estimates. According to FEMA, as of the middle of July 2007, an additional 1,916 project worksheets were in process (these projects are in addition to the 67,253 approved project worksheets mentioned above). FEMA expects that another 2,730 project worksheets will be written. FEMA expects these worksheets to increase the total cost by about \$2.1 billion, resulting in a total expected PA cost of about \$10.3 billion.

Some state and local officials have also expressed concerns about unrealistically low cost estimates contained in project worksheets, which could lead to even higher than anticipated costs to the federal government. A senior official within the Louisiana Governor's Office of Homeland Security and Emergency Preparedness recently testified that some of the projects were underestimated by

a factor of 4 or 5 times compared to the actual cost.¹² For example, the lowest bids on 11 project worksheets for repairing or rebuilding state-owned facilities, such as universities and hospitals, totaled \$5.5 million while FEMA approved \$1.9 million for these projects.

The extent to which the number of new project worksheets and actual costs that exceed estimated costs will result in demands for additional federal funds remains unknown. In addition PA costs may increase until a disaster is closed, which can take many years in the case of a catastrophic disaster.¹³ For instance, PA costs from the Northridge earthquake that hit California in January 1994 have not been closed out more than 13 years after the event. Our ongoing work on the PA program will provide insights into efforts to complete infrastructure projects, the actual costs of completed projects, and the use of federal funds to complete PA projects.

Additional Resource Demands Anticipated for CDBG Program

HUD's CDBG program provides funding for neighborhood revitalization and housing rehabilitation activities, affording states broad discretion and flexibility in deciding how to allocate these funds and for what purposes. Congress has provided even greater flexibility when allocating additional CDBG funds to affected communities and states to help them recover from presidentially-declared disasters, such as the Gulf Coast hurricanes.¹⁴ To date, the affected Gulf Coast states have received \$16.7 billion in CDBG funding from supplemental appropriations—so far, the largest federal provider of long-term Gulf Coast rebuilding funding.¹⁵ As shown in figure 2, Louisiana and Mississippi were allocated the largest shares of the CDBG appropriations, with \$10.4 billion allocated to Louisiana, and another \$5.5 billion allocated to Mississippi. Florida, Alabama, and Texas received the remaining share of CDBG funds.¹⁶

¹²Testimony before the Ad Hoc Subcommittee on Disaster Recovery of the U.S. Senate Committee on Homeland Security and Government Affairs, July 10, 2007.

¹³A disaster is considered to be closed when all projects are approved, all appeals are resolved, and all funds are obligated.

¹⁴CDBG funds supported recovery efforts in New York City following the terrorist attacks of September 11, 2001; in Oklahoma City following the bombing of the Alfred Murrah Building in 1995; and in the city and county of Los Angeles following the riots of 1992.

¹⁵Pub. L. No. 109-148, 119 Stat. 2680, 2779-80 (Dec. 30, 2005); Pub. L. No. 109-234, 120 Stat. 418, 472-73 (June 15, 2006).

¹⁶Texas received more than \$503 million, Florida received about \$183 million, and Alabama received nearly \$96 million. HUD Notice of Allocations and Waivers 71 *Fed. Reg.* 7666 (Feb. 13, 2006); 71 *Fed. Reg.* 63,337 (Oct. 30, 2006).

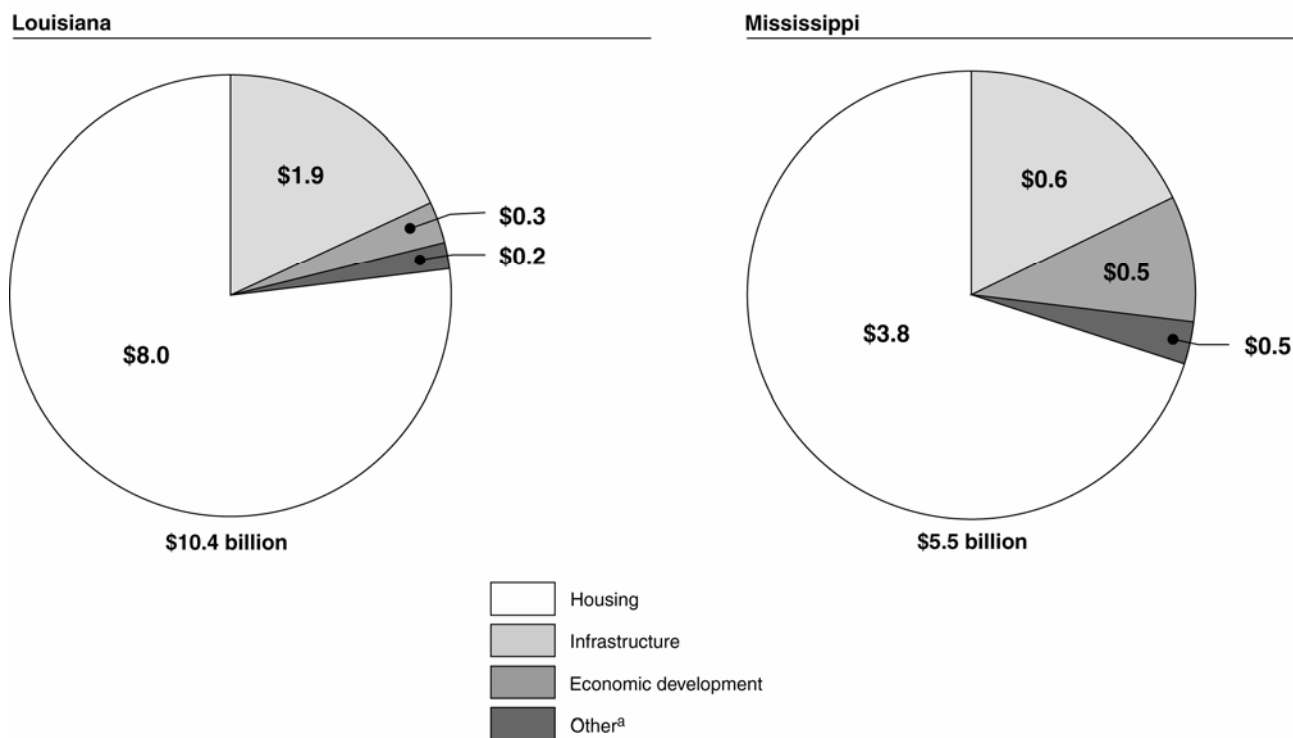
Figure 2: Breakdown of Total CDBG Allocations to Gulf Coast States



Source: GAO analysis of Louisiana Recovery Authority and Mississippi Development Authority.

To receive CDBG funds for Gulf Coast rebuilding, HUD required that each state submit an action plan describing how the funds would be used, including how the funds would address long-term “recovery and restoration of infrastructure.” Accordingly, the states had substantial flexibility in establishing funding levels and designing programs to achieve their goals. As shown in figure 3, Mississippi set aside \$3.8 billion to address housing priorities within the state while Louisiana dedicated \$8 billion for its housing needs.

Figure 3: Most CDBG Funding Allocated to Housing Needs in Louisiana and Mississippi



Source: GAO analysis of agency-provided data.

Note: Totals may not add due to rounding.

^aIn Mississippi, "other" refers to wind insurance mitigation and funds not yet programmed by the state. In Louisiana, "other" refers to funding for planning and administrative activities.

Each state also directed the majority of its housing allocations to owner-occupied homes and designed a homeowner assistance program to address the particular conditions in their state. As discussed below, each state used different assumptions in designing its programs, which in turn affects the financial implications for each state.

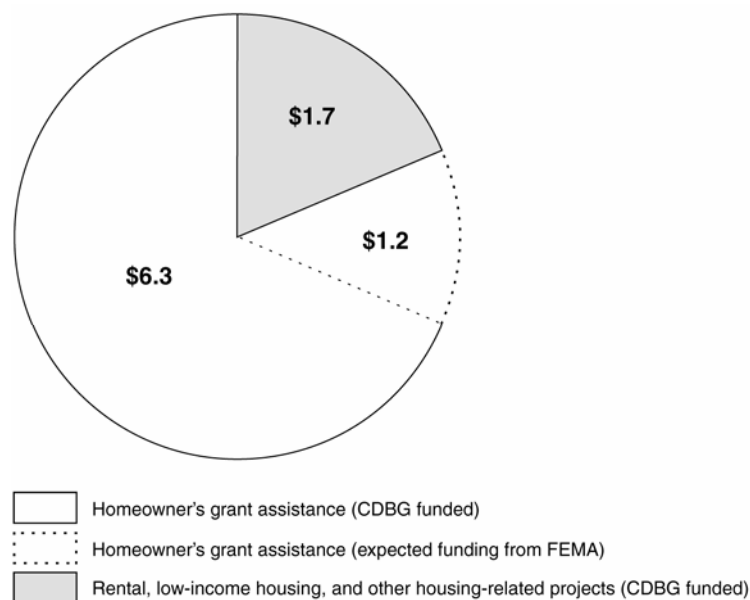
Louisiana's Homeowner Assistance Program Anticipates Shortfall

Using \$8.0 billion in CDBG funding, the Louisiana Recovery Authority (LRA) developed a housing assistance program called the Road Home to restore the housing infrastructure in the state.¹⁷ As shown in figure 4, Louisiana set aside

¹⁷The LRA was created at the direction of Governor Blanco by executive order in October of 2005 and subsequently authorized by the state legislature in early 2006.

about \$6.3 billion of these funds to develop the homeowner assistance component of the program and nearly \$1.7 billion for rental, low-income housing, and other housing-related projects. Louisiana anticipated that FEMA would provide the homeowner assistance component with another \$1.2 billion in grant assistance. Louisiana based these funding amounts on estimates of need within the state. Accordingly, Louisiana estimated that \$7.5 billion would be needed to assist 114,532 homeowners with major or severe damage. Louisiana also estimated these funds would provide an average grant award of \$60,109 per homeowner.

Figure 4: Louisiana's Estimated Funding Distribution for Homeowner Assistance (billions of dollars)



Source: Louisiana Recovery Authority data.

The LRA launched the Road Home homeowner assistance program in August 2006. Under the program, homeowners who decide to stay in Louisiana and rebuild are eligible for the full amount of grant assistance—up to \$150,000. Aside from the elderly, residents who choose to sell their homes and leave the state will have their grant awards reduced by 40 percent, while residents who did not have insurance at the time of the hurricanes will have their grant awards reduced by 30 percent. To receive compensation, homeowners must comply with applicable code and zoning requirements and FEMA advisory base flood elevations when rebuilding and agree to use their home as a primary residence at some point during a 3-year period following closing. Further, the amount of

compensation that homeowners can receive depends on the value of their homes before the storms and the amount of flood or wind damage that was not covered by insurance or other forms of assistance.

As of July 16, 2007, the Road Home program had received 158,489 applications and had held 36,655 closings with an average award amount of \$74,216. With the number of applications exceeding initial estimates and average award amounts higher than expected, recent concerns have been raised about a potential funding shortfall and the Road Home program's ability to achieve its objective of compensating all eligible homeowners. Concerns over the potential shortfall have led to questions about the Road Home program's policy to pay for uninsured wind damage instead of limiting compensation to flood damage. In recent congressional hearings, the Executive Director of the LRA testified that the Road Home program will require additional funds to compensate all eligible homeowners, citing a higher than projected number of homeowners applying to the program, higher costs for homeowner repairs, and a smaller percentage of private insurance payouts than expected.

According to the Federal Coordinator for Gulf Coast Rebuilding, CDBG funds were allocated to Louisiana on the basis of a negotiation with the state conducted between January and February 2006. That negotiation considered the provision of federal funding for the state's need to conduct a homeowner assistance program covering homes that experienced major or severe damage from flooding. The state requested the allocation of federal funding at that time to expand the program to assist homeowners who experienced only wind damage. That request to provide federal funds to establish a homeowner program for homes which only experienced wind damage was denied, as were similar requests from Gulf Coast states such as Texas. The Administration requested the negotiated amount from Congress on February 15, 2006, Congress approved that amount, and it was signed into law by the President on June 15, 2006. Subsequently, Louisiana announced the expansion of the Road Home program to cover damage exclusively from wind regardless of the stated intention of the federal allocation, but fully within their statutory authority.

In addition, the Executive Director of the LRA testified that Louisiana had not received \$1.2 billion in funds from FEMA—assistance that had been part of the Road Home program's original funding design. Specifically, the state expected FEMA to provide grant assistance through its Hazard Mitigation Grant Program (HMGP)—a program that generally provides assistance to address long-term

community safety needs.¹⁸ Louisiana had planned to use this funding to assist homeowners with meeting elevation standards and other storm protection measures, as they rebuilt their homes.¹⁹ However, FEMA has asserted that it cannot release the money because the Road Home program discriminates against younger residents. Specifically, the program exempts elderly recipients from the 40 percent grant reduction if they choose to leave the state or do not agree to reside in their home as a primary residence at some point during a 3-year period.

Although we have not assessed their assumptions, recent estimates from the Road Home program²⁰ and Louisiana's state legislative auditor's office have estimated a potential shortfall in the range of \$2.9 billion to \$5 billion.

While these issues will not be immediately resolved, they raise a number of questions about the potential demands for additional federal funding for the states' rebuilding efforts. Our ongoing work on various aspects of the CDBG program—including a review of how the affected states developed their funding levels and priorities—will provide insights into these issues.

Mississippi's Homeowner Assistance Program Proceeding in Two Phases

In Mississippi, Katrina's storm surge destroyed tens of thousands of homes, many of which were located outside FEMA's designated flood plain and not covered by flood insurance. Using about \$3 billion in CDBG funds, Mississippi developed a two-phase program to target homeowners who suffered losses due to the storm surge. Accordingly, Phase I of the program was designed to compensate homeowners whose properties were located outside the floodplain and had maintained hazard insurance at a minimum.²¹ Eligible for up to \$150,000 in compensation, these homeowners were not subject to a requirement to rebuild. Phase II of the program is designed to award grants to those who received flood surge damage, regardless of whether they lived inside or outside the flood zone

¹⁸Authorized under section 404 of the Stafford Act, the HMGP provides grants to states, which in turn provide funds to eligible applicants to implement measures that substantially reduce the risk of future damages, hardship, loss, or suffering in an area affected by a major disaster. 42 U.S.C. § 5172c.

¹⁹Specifically, the Road Home program would use HMGP funds to provide homeowners with elevation grants of up to \$30,000 and up to \$7,500 for individual storm protection measures such as storm shutters.

²⁰These estimates were developed by ICF International, Incorporated, a company under contract with the state of Louisiana to administer the Road Home program.

²¹To receive an award, eligible applicants must place a covenant on their property, providing that flood insurance and hazard insurance will be maintained in perpetuity, the home will be rebuilt or repaired to local building codes, and if rebuilt, the home will be elevated to FEMA elevation standards.

or had maintained insurance on their homes. Eligible applicants must have an income at or below 120 percent of the Area Median Income (AMI). Eligible for up to \$100,000 in grant awards, these homeowners are not subject to a requirement to rebuild.²² In addition, homeowners who do not have insurance will have their grant reduced by 30 percent, although this penalty does not apply to the “special needs” populations as defined by the state (i.e., elderly, disabled, and low-income).²³

As of July 18, 2007, Mississippi had received 19,277 applications for Phase I of its program and awarded payments to 13,419 eligible homeowners with an average award amount of \$72,062. In addition, Mississippi had received 7,424 applications for Phase II of its program and had moved an additional 4,130 applications that did not qualify for Phase I assistance to Phase II. The State had awarded 234 grants to eligible homeowners in Phase II with an average award amount of \$69,448.

Substantial Losses Affect National Flood Insurance Program Ability to Repay

The National Flood Insurance Program (NFIP) incurred unprecedented storm losses from the 2005 hurricane season. NFIP estimated that it had paid approximately \$15.7 billion in flood insurance claims as of January 31, 2007, encompassing approximately 99 percent of all flood claims received.²⁴ The intent of the NFIP is to pool risk, minimize costs and distribute burdens equitably among those who will be protected and the general public.²⁵ The NFIP, by design, is not actuarially sound because Congress authorized subsidized insurance rates for some policyholders. Until recent years, the program was largely successful in paying its expenses with premium revenues—the funds paid by policyholders for their annual flood insurance coverage. In most years—since its inception in 1968—the NFIP paid for flood losses and operating expenses

²²To receive an award, eligible applicants—similar to those in Phase I—must place a covenant on their property, stipulating that (1) flood insurance will be maintained in perpetuity, (2) the home will be rebuilt or repaired to local building codes, and (3) if rebuilt, the home will be elevated to FEMA elevation standards.

²³“Low-income” homeowners are those with incomes at or below 60 percent of the AMI—which ranges by county.

²⁴See GAO, *National Flood Insurance Program: Preliminary Views on FEMA’s Ability to Ensure Accurate Payments on Hurricane-Damaged Properties*, [GAO-07-991T](#) (Washington, D.C.: June 12, 2007); and GAO, *National Flood Insurance Program: New Processes Aided Hurricane Katrina Claims Handling, but FEMA’s Oversight Should Be Improved*, GAO-07-169 (Washington, D.C.: Dec. 15, 2006).

²⁵42 U.S.C. § 4001(d); 42 U.S.C. § 4016.

with policy premium revenues, rather than tax dollars. However, because the program's premium rates have been set to cover losses in an average year based on program experience that did not include any catastrophic losses, the program has been unable to build sufficient reserves to meet future expected flood losses.²⁶ Historically, the NFIP has been able to repay funds borrowed from the Treasury to meet its claims obligations. However, the magnitude and severity of losses from Hurricane Katrina and other 2005 hurricanes required the NFIP to obtain borrowing authority of \$20.8 billion from the Treasury, an amount NFIP will unlikely be able to repay while paying future claims with its current premium income of about \$2 billion annually.

In addition to the federal funding challenge created by the payment of claims, key concerns raised from the response to the 2005 hurricane season include whether or not some property-casualty insurance claims for wind-related damages were improperly shifted to NFIP at the expense of taxpayers. For properties subjected to both high winds and flooding, determinations must be made to assess the damages caused by wind, which may be covered through a property-casualty homeowners policy, and the damages caused by flooding, which may be covered by NFIP.²⁷ Disputes over coverage between policyholders and property-casualty insurers from the 2005 hurricane season highlight the challenges of determining the appropriateness of claims for multiple-peril events. NFIP may continue to face challenges in the future when servicing and validating flood claims from disasters such as hurricanes that may involve both flood and wind damages. Our ongoing work addresses insurance issues related to wind versus flood damages, including a review of how such determinations are made, who is making these determinations and how they are regulated, and the ability of FEMA to verify the accuracy of flood insurance claims payments based on the wind and flood damage determinations.

Billions Appropriated for Gulf Coast Hurricane Protection Projects

Congress has appropriated more than \$8 billion to the U.S. Army Corps of Engineers (Corps) for hurricane protection projects in the Gulf Coast. These funds cover repair, restoration and construction of levees and floodwalls as well as other hurricane protection and flood control projects. These projects are

²⁶See GAO, *Flood Insurance: Information on the Financial Condition of the National Flood Insurance Program*, GAO-01-992T (Washington, D.C.: July 19, 2001).

²⁷Property owners in certain coastal regions subject to hurricanes and flooding may have to purchase at least two, and sometimes more, different types of insurance policies. Flood insurance is offered by NFIP, while insurance for wind-related damages is generally offered by private insurance companies or state-sponsored insurers. NFIP was established in 1968 in part to provide some insurance protection for flood victims because the private insurers were and still are largely unwilling to insure for flood risks.

expected to take years and require billions of dollars to complete.²⁸ Estimated total costs for hurricane protection projects are unknown because the Corps is also conducting a study of flood control, coastal restoration, and hurricane protection measures for the southeastern Louisiana coastal region as required by the 2006 Energy and Water Development Appropriations Act²⁹ and Department of Defense Appropriations Act.³⁰ The Corps must propose design and technical requirements to protect the region from a Category 5 hurricane.³¹ According to the Corps, alternatives being considered include a structural design consisting of a contiguous line of earthen or concrete walls along southern coastal Louisiana, a nonstructural alternative involving only environmental or coastal restoration measures, or a combination of those alternatives. The Corps' final proposal is due in December 2007. Although the cost to provide a Category 5 level of protection for the southeastern Louisiana coastal region has not yet been determined, these costs would be in addition to the more than \$8 billion already provided to the Corps.

Restoring Louisiana's Wetlands and Barrier Islands Will Likely Cost Billions

The Corps' December 2007 proposal will also influence future federal funding for coastal wetlands and barrier islands restoration. Since the 1930s, coastal Louisiana lost more than 1.2 million acres of wetlands, at a rate of 25–35 square miles per year, leaving the Gulf Coast exposed to destructive storm surge. Various preliminary estimates ranging from \$15 billion to \$45 billion have been made about the ultimate cost to complete these restoration efforts. However, until the Corps develops its plans and the state and local jurisdictions agree on what needs to be done, no reliable estimate is available. We are conducting work to understand what coastal restoration alternatives have been identified and how these alternatives would integrate with other flood control and hurricane protection measures, the challenges and estimated costs to restore Louisiana's coastal wetlands, and the opinions of scientists and engineers on the practicality and achievability of large-scale, comprehensive plans and strategies to restore coastal wetlands to the scale necessary to protect coastal Louisiana.

²⁸See GAO, *Hurricane Katrina: Strategic Planning Needed to Guide Future Enhancements Beyond Interim Levee Repairs*, [GAO-06-934](#) (Washington, D.C.: Sept. 6, 2006); and GAO, *U.S. Army Corps of Engineers' Procurement of Pumping Systems for the New Orleans Drainage Canals*, [GAO-07-908R](#) (Washington, D.C.: May 23, 2007).

²⁹Pub. L. No. 109-103, 119 Stat. 2247, 2247 (Nov. 19, 2005).

³⁰Pub. L. No. 109-148, 119 Stat. 2680, 2761 (Dec. 30, 2005).

³¹Pub. L. No. 109-103, 119 Stat. 2247, 2248.

GO Zone Tax Incentives Provide Assistance for Recovery

The Gulf Opportunity Zone Act of 2005 provides tax benefits to assist in the recovery from the Gulf Coast hurricanes.³² From a budgetary perspective, most tax expenditure programs, such as the GO Zones, are comparable to mandatory spending for entitlement programs, in that federal funds flow based on eligibility and formulas specified in authorizing legislation.³³ The 5-year cost of the GO Zones is estimated at \$8 billion and the 10-year cost is estimated to be \$9 billion. Since Congress and the President must change substantive law to change the cost of these programs, they are relatively uncontrollable on an annual basis. The GO Zone tax benefits chiefly extend, with some modifications, existing tax provisions such as expensing capital expenditures, the Low Income Housing Tax Credit (LIHTC), tax exempt bonds, and the New Markets Tax Credit (NMTC). The 2005 Act increases limitations in expensing provisions for qualified GO Zone properties. The Act also increased the state limitations in Alabama, Louisiana, and Mississippi on the amount of LIHTC that can be allocated for low-income housing properties in GO Zones. Further, the act allows these states to issue tax-exempt GO Zone bonds for qualifying residential and nonresidential properties. Finally, the NMTC limitations on the total amount of credits allocated yearly were also increased for qualifying low-income community investments in GO Zones.

We have a congressional mandate to review the practices employed by the states and local governments in allocating and utilizing the tax incentives provided in the Gulf Opportunity Zone Act of 2005. We have also issued reports on the tax provisions, such as LIHTC and NMTC, now extended to the GO Zones by the 2005 Act.³⁴

Observations

Rebuilding efforts in the Gulf Coast continue amidst questions regarding the total cost of federal assistance, the extent to which federal funds will address the rebuilding demands of the region, and the many decisions left to be made by

³²Pub. L. No. 109-135.

³³Tax expenditures may substitute for a federal spending program in that the federal government “spends” some of its revenue on subsidies by forgoing taxation on some income. See GAO, *Government Performance and Accountability: Tax Expenditures Represent a Substantial Federal Commitment and Need to Be Reexamined*, [GAO-05-690](#) (Washington, D.C.: Sept. 23, 2005).

³⁴See GAO, *Tax Credits: Opportunities to Improve Oversight of the Low-income Housing Program*, [GAO/T-GGD/RCED-97-149](#) (Washington, D.C., Apr. 23, 1997); and GAO, *Tax Policy: New Markets Tax Credit Appears to Increase Investment by Investors in Low-Income Communities, but Opportunities Exist to Better Monitor Compliance*, [GAO-07-296](#) (Washington, D.C.: Jan. 31, 2007).

multiple levels of government. As residents, local and state leaders and federal officials struggle to respond to these questions, their responses lay a foundation for the future of the Gulf Coast. As states and localities continue to rebuild, there are difficult policy decisions that will confront Congress about the federal government's continued contribution to the rebuilding effort and the role it might play over the long-term in an era of competing priorities. Congress will be faced with many questions as it continues to carry out its critical oversight function in reviewing funding for Gulf Coast rebuilding efforts. Our ongoing and preliminary work on Gulf Coast rebuilding suggests the following questions:

How much could it ultimately cost to rebuild the Gulf Coast and how much of this cost should the federal government bear?

How effective are current funding delivery mechanisms—such as PA and CDBG—and should they be modified or supplemented by other mechanisms?

What options exist to effectively build in federal oversight to accompany the receipt of federal funds, particularly as federal funding has shifted from emergency response to rebuilding?

How can the federal government further partner with state and local governments and the nonprofit and private sectors to leverage public investment in rebuilding?

What are the “lessons learned” from the Gulf Coast hurricanes, and what changes need to be made to help ensure a more timely and effective rebuilding effort in the future?

Mr. Chairman and Members of the committee, this concludes my statement. I would be happy to respond to any questions you may have at this time.

GAO Contact and Staff Acknowledgments

For information about this testimony, please contact Stanley J. Czerwinski, Director, Strategic Issues, at (202) 512-6806 or czerwinski@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Individuals making key contributions to this testimony include Kathleen Boggs, Peter Del Toro, Jeffrey Miller, Carol Patey, Brenda Rabinowitz, Michelle Sager, and Robert Yetvin.

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